

MINUTES  
REGULAR MEETING OF BOARD OF LAND COMMISSIONERS

June 19, 2006, at 9:00 a.m.  
Room 303 State Capitol Building  
Helena, Montana

PRESENT: Governor Brian Schweitzer, Secretary of State Brad Johnson, Attorney General Mike McGrath, Superintendent of Public Instruction Linda McCulloch, and State Auditor John Morrison

Mr. Johnson moved for approval of the minutes from the May 15, 2006, meeting of the Board of Land Commissioners. Seconded by Mr. Morrison. Motion carried unanimously.

**BUSINESS CONSIDERED:**

606-1      REQUEST TO SET MINIMUM BID FOR GARFIELD COUNTY LAND BANKING PARCELS

Ms. Sexton said this is a request to set the minimum bid amount for Garfield County land banking parcels. In May 2005, the Board approved 32 isolated and lessee-nominated parcels totaling 9,600 acres in Garfield County. The department proposes setting the minimum bid for these parcels totaling 7,040 acres which brings the present acres offered for sale across the state to 19,824 acres. There is a list of the appraisals in the Board's packet. They vary with and without access, the lowest without access is at \$90 and the highest with access is at \$345 per acre. Again, the total acreage in Garfield County is 7,040 acres and the estimated revenue at the minimum bid and that is assuming access is \$998,000. This will be the last large segment of acres that will be passing for minimum bid. We will then go out and set a date, I believe it is October 5, 2006, for the sale of these parcels.

Motion was made by Mr. McGrath to approve the minimum bid for parcels in Garfield County. Seconded by Mr. Johnson and Ms. McCulloch simultaneously. Motion carried unanimously.

606-2      REQUEST FOR FINAL APPROVAL TO SELL LAND BANKING PARCEL #372

Ms. Sexton said I take great pleasure in presenting this to you. On June 20, 2005, the Board gave preliminary approval for the sale of #372, Spring Prairie, this is Section 36 just north of Kalispell, to continue through the land banking process. The Board set the minimum bid in January 2006 at \$41,457 per acre and last Thursday, June 15, 2006, the parcel sold at public auction in Kalispell. The high bid for the parcel was by West Homes and it was for \$75,117 per acre for a total sale price of \$6.4 million. I want to add also, this is not just for the 85.2 acres but also includes the legal access from Four Mile Drive and Tree Line Drive. That was omitted from the information item, but the legal access is included. It is the recommendation of the department that the Board finally approve the first land banking parcel, #372, at Spring Prairie for \$6.4 million. I want to thank the staff and Land Board staffers who attended the auction. It went smoothly and there was lively bidding. This is almost double what the minimum bid was.

MINUTES  
June 19, 2006  
Page 2

Mr. McGrath said I would point out the remarkable disparity between this 606-1 and 606-2. In 606-1 we are setting a minimum bid at \$115 per acre and in 606-2 we are selling land for \$75,000 per acre. It tells a lot about what is happening in Montana.

Governor Schweitzer said it is a very good observation. I think if you look chronologically at the value of range land in Garfield or Rosebud County over the last ten years we might find it may be increasing at 3% - 4% per year versus some of these western Montana values.

Motion was made by Mr. Johnson to approve the sale of #372. Seconded by Mr. McGrath. Motion carried unanimously.

606-3      AUTHORIZATION FOR PROPOSED ACQUISITION OF HERITAGE PROPERTY

Ms. Sexton said this is a request for authorization for a proposed heritage property. This is under the provisions of the Montana Heritage and Development Commission. They requested the Board grant approval to accept a donation of heritage property known as the Pioneer Cabin on Last Chance Gulch. This acquisition would address the Commission's legislative mandate to seek heritage properties and the economies of scale associated with managing the adjacent properties, such as Reeder's Alley. I am turning this over to Jeff Tiberi from the Department of Commerce, and I believe there are also representatives here of the Last Chance Gulch Restoration Association who are the current owners.

Jeff Tiberi, Commerce, said I was here about six years ago with Reeder's Alley where the owner of Reeder's Alley offered that as a donation to the State of Montana, the Board approved that and we have managed it since. We've tried to be a good neighbor to the Pioneer Cabin right adjacent to our property and work with the Last Chance Gulch Restoration Association. In 2004 they came and said would you be interested in taking this property as a donation. We explored that. The report is submitted in our agenda item. We are very happy that they approached us and we think this is a vehicle for long term preservation of the Pioneer Cabin. We are hoping you will give it a "yes" vote.

Governor Schweitzer said oftentimes folks will donate to us a parcel and it becomes a liability for the rest of time, some of our historic sites are drains on our economy. They are unlike some other assets of the State of Montana. I see there are some provisions, would you talk about those?

Mr. Tiberi said there are two main properties, the Pioneer Cabin proper and the caretaker's cottage. The caretaker's cottage is rented out, we get a monthly rent from it. We are examining different approaches for that perhaps how to use that in a different way and to take care of the whole property. Plus there is an endowment that is owned by the Montana Community Foundation and the state would become the beneficiaries of that endowment. It is about \$58,000. We would get the annual interest from that. Between those two regular incomes coming in plus the opportunity for grant programs because of the nature of the site, and the condition of the site which was looked at by the State Historic Preservation officer historical architect (and its in pretty good condition for the age) we feel comfortable that we will be able to move forward. We have a track record on Reeder's Alley where the same question was posed about the care of that and we have a balance in that account of about \$60,000 at this point for when something major breaks. We are comfortable we will be able to take care of it.

Motion was made by Ms. McCulloch to approve the acquisition of heritage property. Seconded by Mr. Morrison. Motion carried unanimously.

606-4      APPROVAL FOR THE JUNE 6, 2006, OIL AND GAS LEASE SALE

Ms. Sexton said we held our oil and gas lease sale on June 6, 2006, at the Scott Hart Building auditorium. A total of 279 tracts were offered for lease. They were leased for a total of \$1,791,370 and the sale covered a total of 123,000 acres, the average bid was \$14.54. The high bid went to Richland County and this was actually a small acreage piece owned by FWP which we do work with FWP in leasing. The total income for the year from oil and gas mineral income has been \$38.5 million. We are looking at a year end total of probably over \$40 million which will be one of the highest. We can't say it will be the highest at this point in time because we don't know, but it will certainly challenge that category. I have a breakdown. Most of this, \$1.7 million, went to common schools, the remainder went to other trust beneficiaries including the FWP beneficiary.

Motion was made by Mr. Morrison to approve the oil and gas lease sale. Seconded by Mr. McGrath. Motion carried unanimously.

606-5      ADOPTION OF POLICIES:  
A.      ACCESS ROAD POLICY  
B.      RECIPROCAL ACCESS AND EASEMENT EXCHANGE POLICY

Ms. Sexton said this is in two parts. These are two different policies, the access road policy and the reciprocal access and easement exchange policy. We've been working on these for some months to update them and look at values for the trust so we are gaining the best value we can in working with our cooperators in the reciprocal access as well as the access road policy. The two components I want to particularly point out are the Road User's Association which is established through this policy and the conveyance fee.

David Groeschl, DNRC Forest Management Bureau Chief, said before you today are two policies that deal with access or easements. The first policy is the access policy that deals with the granting of easements across state lands and the second policy is the reciprocal access policy that deals when there is an exchange of easements between the state and a cooperator. We look to get equal value in that exchange. The reason for these policies as far as the revisions and drafting these is (1) to address and clarify the process internally for how we put these packages together and what constitutes either just a straight grant of an easement versus what is a reciprocal or exchange of easements, and (2) the reason for revising the policy was to look at the valuation and to have our policy consistent with what other states around us were doing as well. Looking at the two policies there is a little bit of a difference between the two in that the access policy where we grant easements across state lands, for example for a driveway, you can have anything from a term easement from 5, 10, 15, 20, 30 years to a perpetual easement. In the reciprocal policy because we are granting easements, we are exchanging easements with a cooperator and we would like to have permanent easements, those easements we grant across state lands are perpetual easements and are for all lawful purpose. So we grant all lawful purpose perpetual easements and we receive all lawful purpose perpetual easements in that situation. The other distinction between the access and reciprocal policy is the access policy, since it is for driveways and typically it is to a single housing unit on a lot, the standard is a 30-foot wide easement that is granted. If additional width is desired by the other party that wants access, they can purchase additional width. So if they are going to put in a subdivision or something later on, they would pay for that additional width up to 60 foot. In the reciprocal policy since we are granting perpetual easements that are for all lawful purpose the standard there is a 60-foot right-of-way width we are granting and receiving. Again, since we are exchanging

MINUTES  
June 19, 2006  
Page 4

easements in that situation we are trying to have like terms for the policy. Those are some of the distinctions between the two.

Governor Schweitzer said what we're saying is we're building a menu for what you're using this easement for. If you're building an easement to something other than traditional uses in this reciprocal versus say timber management or range management or agriculture then it opens up a new discussion.

Mr. Groeschl said yes. I should have pointed out the real trigger especially in the reciprocal access policy is that if the state enters into exchange easements with another party and either the state or the other party decides to sell a parcel out of that tributary area that's in the reciprocal access package, let's say we have a 10,000-acre tributary area where we're exchanging easements with each other where we have mutual access needs, once we exchange those easements, if one or the other party decides to sell a part of that tributary area, say 100 acres, and they are going to subdivide it, then it triggers two things. It triggers the formation of a road user's association to maintain the maintenance on that because there is additional wear and tear on that road. The other thing it does is there is a conveyance fee that kick in depending upon how many lots. So if that 100 acres is divided into ten lots, a conveyance fee is charged per lot. In the reciprocal policy it identifies the counties where there is a \$500 per lot fee versus all other counties that are \$250 per lot. If they subdivide it and sell those lots, they form a road user's association and they pay the conveyance fee. If the land is not sold and the cooperator retains the underlying ownership but decides to develop it and put some condos on it or whatever, before it goes to final subdivision plat, before the final plat is approved, they would also have to pay that conveyance fee. Regardless if the land changes ownership or is retained by the original cooperator, if it is subdivided there is a conveyance fee paid. And that works both ways. The state would pay the cooperator that conveyance fee if it subdivides and puts development, cabin site leases or whatever, on state lands. It works both ways.

Mr. Johnson said I think the potential exists for the state to get upside down in some of these reciprocal agreements if in fact a timber company comes in and wants a 30-foot easement for six months to get the sale done and we expect a reciprocal arrangement and we are going to insist on 60 feet and perpetual easement, etc. Just looking at the example here of a timber company's easement going in at \$5,600 and if we simply go to the second box and insist on a reciprocal that is 60-feet, we're going to be obligated for \$15,000 while they are in this for \$5,600. Ultimately that balance sheet is going to have to be brought to even. Where in the case of those shortfalls will those revenues come from within the department?

Mr. Groeschl said when we develop a reciprocal access agreement with another party there are several components. One, we look at what the underlying land value is that that road prism lays on. So for each segment of road that's on either the cooperator or the state we come up with a land value and a road value to address the fair market value of that easement. We try to balance that out as much as we can within the tributary area depending upon the acres in the tributary area, the length of road, and we try to balance the difference out between the state and the cooperator. Typically, we are always looking for more access. We are typically receiving more access than what we are granting and typically there is a balance due that the state owes the cooperator. The land value, the difference that is owed, we pay out of what is called the Forest Improvement Fee (FIF) which under statute is part of that fee is used to purchase access to state land. If there is either a direct purchase or a balance due on a reciprocal access package we use money out of FIF to pay that balance off. That is where the money would come from and we try to balance it when we put the package together.

Mr. Johnson said how is FIF funded? Is it general fund money? School trust money?

Mr. Groeschl said the FIF is state special revenue. It is a fee charged when we sell a timber sale the bidder submits a stumpage rate and in the sale prospectus there is a FIF that is calculated and it is by land office. If they bid on a sale in the Northwestern Land Office or the Southwestern Land Office, there is an FIF that is charged and it is right now about \$10/ton. It varies by land office. There is a FIF charged, it goes into the FIF account and out of that account we pay for things such as access, pre-commercial thinning, planting, those sorts of activities.

Governor Schweitzer said it seems to me if a company, any company – Apple Creek Land Company – has been doing exchanges with the State of Montana and if the Apple Creek Company does an easement exchange with the State of Montana and they ultimately subdivide that 640 acres and now there are 100 homesites there, they will pay a substantial sum sometime in the future back into this pool. Correct?

Mr. Groeschl said yes that's correct.

Governor Schweitzer said the more likely scenario in many cases across western Montana is that the company does not build a bunch of condos in the corridors next to the wilderness but that they subdivide it into 40's or 160's. Once they are divided into those 40's or 160's there is a subtle change in the management of that land. The subtle change is that instead of managing that land for timber resources and those timber resources providing jobs to a lot of people around, there will be some trophy homes built, some guest homes, a few ponds for private lakes and a few other things. But if you divide 640 acres just four ways, the amount of revenue that accrues is very small relative to the lost opportunity of managing that as a timber land and having that timber every 80 – 120 years harvested and hauled to a local mill. It seems to me that this begins to address the concerns that some of us have had but maybe doesn't get exactly to the entire issue because in many cases in western Montana land is worth more in a tract of 40 or 160 acres than it was broken into five- or ten-acre tracts. I don't know if this policy addresses it unless I am missing something.

Mr. Groeschl said we tried to look at what a reasonable fee would be given that we look at how these parcels are changing ownership and how they are being broken into smaller and smaller parcels. We recognize the fact in many many areas where we manage timber lands that as that land ownership changes, as it gets broken into smaller parcels, that it becomes more difficult to manage. More people want to have a say on how it is managed, the view shed on how it is managed, and we've tried to strike a balance on the fee that is charged for this and tried to make it equitable so both parties recognize that there is an additional burden not only with wear and tear on the road but some lost opportunity for managing those. It becomes more costly at times to manage because there are involvement and folks that want to maintain the view shed. We tried to strike a balance based on that.

Governor Schweitzer said my concern is the term reciprocal. I think many of those on the Board along with me recognize the special nature of managing a legacy. In the case of timber lands we know our job is to manage them for sustainable timber harvest, much less and maybe even to the point of zero, managing them for their development potential versus some companies that are our neighbors who are increasingly viewing their timber lands as development land. So is it reciprocal? That is my concern from the beginning, is it truly reciprocal when our intent and our management technique is to manage that for grazing, timber, and for long term ownership versus any private owners who are actually currently reviewing a plan of dividing it, maybe not into condominiums or apartments or multiple houses, but into these 160's and 320's? I don't know it is reciprocal when we have a different mission than they have.

Tom Schultz, DNRC Trust Land Management Division Administrator, said I just want to address your point. In the initial policy that went out for public comment we tried to get into that perspective you are

MINUTES  
June 19, 2006  
Page 6

talking about. Instead of assuming a plat will address all of the issues, you're right, it could be a 160 acres, it could be 140, or 320, it could be the entire 640 acres as we've seen in Whitefish where the larger tract the more valuable it is. We came up with a defacto 20-acre assumption that we had in the initial policy that said we don't care what the size is, we are going to assume for purposes of the policy we are going to hit you with a 20-acre subdivision regardless of what the plat said. The plat might say one home per 640 acres, we don't care, we are going to do it on a 20-acre basis. We went out for public review. We met with the cooperators several times through our public involvement process and we did get feedback from the cooperators that they thought it would be unworkable. So we did make a change from the initial draft policy that went out to this policy which incorporated public comment to address that. I don't disagree with that, maybe the policy isn't perfect, but I still think our recommendation to pursue down this road cautiously and let us try this based upon what a plat might suggest, whether it's ten lots, two lots, or one lot. We did envision what you're talking about in terms of just assuming a 20-acre lot density at a minimum for each tract regardless of what it was actually broken into but the feedback we got was that that would not be very workable. We did pursue that and we did get public comment to the contrary on that and you'll probably hear from the cooperators today.

Mr. Johnson said how much, if we implement this as presented, how much are we limiting the latitude with regard to negotiations on a case-by-case basis? I can see instances where going through all you have to to establish perpetual reciprocal easements is maybe not going to be appropriate. The kind of thing I am thinking about is salvage timber sale where there is some urgency and the timber company simply wants to be able to get in and get out and be done with it. Are we still going to have the ability to accommodate those folks in those situations?

Mr. Schultz said yes we are. I want to reiterate this policy does not require perpetual easements under the reciprocal policy. What it says is we will exchange with our cooperators what they want to exchange. Most of the cooperators these days have a long term view to long term value. If you talk to most of them they would prefer a perpetual easement. If an emergency situation came up, a fire burn, we would not hinder their ability to get access in the short term, but more than likely if it was an area they wanted to get into, we would work with that cooperator over the long term to get access both for them and for the state. The other thing I want to bring up is you asked about flexibility. One of the other things we have been working on per the Board's direction is we try to negotiate public access as a component of each and every reciprocal access agreement we do. We diligently try to do that. Most cooperators have been willing to work with us. They have not charged us an additional fee for that access. One of the things this policy envisions is if, because now we are charging a conveyance fee, that made it more difficult to get the public access, the Board has the discretion to look at that conveyance fee and maybe view it in light of what else are we getting in addition to this management access, is are we getting public access. And that may weigh into the Board's decision in terms of how to do the conveyance fee. We tried to write that into the policy. We did want to provide the Board with flexibility, we wanted to provide the cooperators with flexibility and at the same time we wanted to address the issues we heard discussed regarding what is the true value and nature of the reciprocal access. Is it for just timber management or is it for some greater value? But the state is getting those rights but it may not act upon those rights in the short term or the long term.

Mr. Morrison said given the questions that have been raised here I think it might be appropriate to table 606-5 and try to iron some of these things out and maybe bring it back next month for final approval.

Ronald Buentemeier, F.H. Stoltze Land and Lumber Company, said Stoltze is the oldest family-run sawmill in Montana. Mr. Stoltze came into the Flathead Valley in the early 1900's. Our first experience with right-of-ways with state land was with logging railroads. Section 16 in Haskill Basin is one of those

in 1914. I worked for the company for 43 years and have had pretty extensive experience with rights-of-ways and the reciprocal process that is currently being used. I'd like to make these comments. We appreciate the cooperation and ability to be involved in the review of these policies provided by the Department of Natural Resources and Conservation. Stoltze and the DNRC enjoy a long history of cooperation with regard to access issues and we look forward to continuing this relationship. Periodic review of policy and procedure is important to keep up with changing times. That being said, we would like to raise the following issues and concerns with regard to the policies presented.

The Land Board and the DNRC must expect to be held to the same high standards, valuation methods, fees and restrictions that these policies propose to impose on private cooperators when the trusts need to acquire access. At least in northwestern Montana, trust lands are generally in need of acquiring access more often than they are granting access, especially when you compare miles of right-of-way granted to miles of right-of-way received. We question whether the potential economic impact to the trusts of some of the proposed requirements has been fully examined. We notice that the briefing you received from the department shows an example of when the trusts grants an easement, however, there is no example when the trust must purchase an easement. Provisions will be necessary to increase budgets for ROW acquisition

There are potential legal and logistical problems with the proposal to assign new or existing easements to Road User's Associations (RUA). These associations are ephemeral in nature and only as good as the paper they are written on. How will DNRC deal with a situation where the RUA becomes defunct? While you may cancel the easement, the reality is that the road will still exist, individual landowners will be unhappy and the DNRC will be stuck with dealing with road maintenance issues and costly legal battles over access. We suggest the requirement of forming an RUA to manage road use, however partially assign easements to individual landowners, i.e., property, to ensure accountability.

Under both policies the term "all lawful purposes" is used when referring to the extent of rights granted and received. There is no discussion in either policy describing what these rights actually include. Are utilities that lie within the right-of-way corridor included in "all lawful purposes" grants? It would seem that additional language may be necessary to describe extent of rights such as "all lawful purposes, including utilities, not including access for the public."

Comments on the Access Road Easement Policy:

It is clear that the Board wishes to retain the option of granting either term or perpetual easements. It would be helpful for there to be some direction in the policy when one should be granted over the other. It is impossible for an applicant to determine this very important fact from the proposed policy. This is too important of an issue to be made without clear procedure and direction.

We understand the preference for the state to operate under reciprocal access or easement exchange. However, there are occasions, especially when the state is not able to fulfill it's responsibility under reciprocity, where a private entity must still be allowed to purchase an easement through the Access Road Easement Policy, even though the potential for reciprocity exists. For example, Stoltze initiated a cooperative access project in the King Creek area, including exchange of access with the DNRC on March 2, 1990. After ten years of working on the project, the DNRC was not able to fulfill it's responsibility under reciprocal access. In October 2000, Stoltze found it necessary to purchase a limited timber management only easement from the state to meet our management needs. To date, the state still has not resolved access issues with three other landowners and does not enjoy full access itself. Since the state must expect to play by the same rules of reciprocity, this example could have been reversed and the

state may have needed to purchase an easement. For these types of situations and others, the ability to outright purchase an easement must be retained both for the state and cooperator.

Reciprocal Access/Easement Exchange Policy Comments:

We fully understand the desire of the Board to acquire the best access possible to trust lands, and agree that the trust should always receive equal rights to what they are granting. However, there will be occasions where it is not in the best interest of the trust to purchase 60 feet all lawful purpose access. The additional cost of acquiring this access may be prohibitive, furthermore, certain cooperators may not be willing to grant "all lawful purposes" across their private lands, especially if they are not requesting the same across state land. We encourage the Board to retain the latitude for exchanging leases rights when necessary. We have found that limited access rights are still better than no access rights, and there will likely be opportunities to improve access if specific future projects warrant additional rights.

We are extremely concerned over the direction of the Board to always attempt to acquire access rights for the public. The Board needs to understand that these rights, especially motorized access rights, will come at a significant cost. As a cooperator, the addition of public access to a reciprocal access project exponentially increases the burden on the private property. The Board will need to expect to bear the cost not only of compensation for the public access right-of-way, but also be willing and able to assume the extra cost associated with increased maintenance resulting from public use. Furthermore, we are perplexed as to why the Board would attempt to acquire motorized access across private lands when in general, the department prohibits motorized use on trust lands! Is it really appropriate to ask a cooperator to allow the public to drive across private lands so the public can park at the gate on trust lands and only hike, bike, or horseback ride from there on trust lands?

We urge the Board to consider the issues we have raised and ask that the department revise the proposed policies to adequately address these concerns. Thank you.

Mr. Johnson said we're faced with a Supreme Court decision that says as a Board we can't discount rights-of-ways to county governments that are maintaining county roads across school trust lands even though a number of us on the Board felt that was a reasonable reciprocal situation. Are we creating any kind of unintended consequence here? Mr. Schultz said we would be able to take into account the intrinsic value of some of these reciprocal situations. Can we really do that or are we going to find ourselves in a situation where we are simply going to have to calculate a dollar and cents number and assess it?

Mr. McGrath said I don't know the answer to that, it depends on the circumstances. The courts require us as trustees to get fair market value for the use of our lands. So the question is, how are we going to be able to determine that? We struggle with that on lots of issues lots of times. I think, at least in part, the idea here is to ensure we do that in the example of a subdivision where access is granted across our land. Not only is it valuable to the subdivision but we have increased costs in terms of maintenance of that land. Mr. Buentemeier mentioned just the opposite of that could happen if we are obtaining access of course across private lands. Those have to be valued in each particular circumstance. That is the idea of the conveyance fee.

Mr. Schultz said we struggled with this internally, this very question. The way the policy is crafted right now the determination of fair market value is limited to the two components Mr. Groeschl spoke to previously. The land value and then the value to actually build or construct the road, the gravel, the materials, the asphalt, the time and the equipment. The conveyance fee as per in the policy, is not a component of fair market value. It is a fee above and beyond fair market value if someone were to do a subdivision or sell a parcel of land at a later point in time. We were very careful in terms of how we



MINUTES  
June 19, 2006  
Page 9

wrote the policy to differentiate the conveyance fee from the determination of fair market value so we would not get into the bind you are talking about where if the Board chose to limit or not even apply a conveyance fee in a particular instance because of some other issue that may have come up like the concept of public access where someone was going to charge us additional for that and the Board maybe decided because of that they waived the conveyance fee. But we really wanted to view the conveyance fee as something outside of the determination of fair market value.

Governor Schweitzer said initially the staff looked at the measures state land was making, not so much in dealing with reciprocal access with our neighbors and partners across western Montana relative to timber harvest and grazing management and to a lesser extent mineral extraction. The concern was that at least some members of this Board don't believe we ought to be in the business of liquidating those state trust lands, we want to maintain them as timber lands. We will continue as you'll see later today issuing contracts to private companies to harvest timber on state lands. There is a multiple use factor in state lands for watershed management, for game management, recreation, and timber management. If I have a neighbor and we have an agreement about a gate between our two properties and we agree they can come in with their pickup to move their cattle out and we can move our cattle out, that's one thing. But if that agreement we made means that that neighbor is going to subdivide that into 160's and I'm going to have a bunch of ranchettes and knapweed culturing centers, then it makes it a much different issue. That's what we're trying to establish here. Stoltze has been in business for a long time in the timber business. Are you going to continue in the timber management business? Is that your intent? Or are you going to be in the business of the other?

Mr. Buentemeier said I stated many times the goal of the Stoltze family as a privately-held company is to continue in the management of our timber lands for timber and to supply wood fiber for our sawmill. Now, I'll paraphrase that with we can only continue to operate that sawmill if we can have some outside sources of logs because the 36,000 acres we own only provides about 25% of our needs for the sawmill. We've got to come to state lands and bid on their timber sales, to other private lands, and to national forests to get that other 75% and that's where the rubber meets the road today. We are really struggling to make that happen. We may in the future sell some land, we've occasionally sold a tract in recent times and taken that money and bought high value lands and more timber lands someplace. We've been fairly successful at that. I am not going to tell you we're not selling some land, but our goal is to continue in the timber business. You have a difficult problem here and I understand what you're trying to get at. I don't have a good solution for you to make that happen. But the Board needs to remember is that on state lands you need a tremendous amount of access in northwest Montana and you don't have that today and its going to get really costly if these rules become onerous to the private landowners.

Governor Schweitzer said the intent here is to enhance opportunities for reciprocal access for similar management techniques. Trying to identify what some of those other management techniques might be outside timber harvest and to adequately assess the value for those opportunities for private landowners. If the State of Montana were wearing the other shoe, let's say we had a Land Board that was so possessed it thought it was in the land liquidation business, in order to raise a lot of money what we ought to do is sell this land, put it in stocks and bonds or some other investments and we can get a much higher return than waiting around for some trees to grow. Under those circumstances you'd expect our neighbors like Stoltze and Plum Creek to say hold on here, just wait a minute these reciprocal agreements were for timber harvest. And any of them we make with you in the future we are going to adequately value based on your intentions to develop that land. That's what we are attempting to do here. If this vehicle is not the correct one, we are going to continue to work on it.

Mr. Buentemeier said the reciprocal access agreements I have with the state I have specifically done that. They are for timber management purposes. In the envision for our company, if we wanted to expand those or if the state wanted to expand those for its purpose we would come back and renegotiate at that time as to what the value should be and what money should transpire. That's a difficult thing and I applaud you for what you're trying to do. But I don't think either of us has a crystal ball to see what is going to happen in the future. For myself, what is happening in the Flathead today, I've lived there most of my life and even ten years ago if you told me that was happening I'd say what kind of wacky weed were you working on.

Mr. McGrath said I would echo what Auditor Morrison said. It may well be given all these questions we ought to take a look at it. I have concerns and I think Mr. Buentemeier pointed them out, about sportsmen's access. One of the things we've worked very hard on in the last five years is to ensure we have public access to state lands and that when we do these kinds of agreements it includes public access. I think we have to make sure, and I think we need more time to look at this in a more depth to make sure we're not putting ourselves in a box in terms of sportsmen's access as well.

Motion was made by Mr. Morrison to table this agenda item for further work. Seconded by Ms. McCulloch. Motion carried unanimously.

606-6      REQUEST FOR APPROVAL OF RIGHTS-OF-WAY APPLICATIONS

Ms. Sexton said this month we have historic rights-of-way for three different utilities, there are a number of access proposals also for telephone and electric utilities, there is one private access road for a clean up of a land banking parcel we have. We did determine if there was any historic access across land banking parcels that neighbors wanted to solidify we would do that and that is what this is, a historic private access road for the River Junction parcel. They are as follows: #13642 from Sheridan Electric Cooperative for an overhead electric distribution line; #13660 from 3 Rivers Communications for a buried telephone distribution line; #13622 through 13628, #13651 through 13658 are from Beartooth Electric Cooperative for overhead electric distribution lines; #13543 and 13644, #13661 through 13663 are from Central Montana Communications for buried electric distribution lines; #13717 through 13728 are from Glacier Electric Cooperative for overhead electric distribution lines; and #13729 is from William and Patricia Fogarty for a private access road to a single family residence and associated outbuildings and to conduct normal farming and ranching activities. Ms. Sexton recommended approval of the rights-of-way requests this month.

Motion was made by Mr. Morrison to approve the applications. Seconded by Mr. Johnson. Motion carried unanimously.

Ms. Sexton requested approval to take into consideration the next five timber sale requests as a package. She said they are smaller sales that amount to a total of 5.6 million board feet.

606-7      RATTLESNAKE CREEK LIMITED ACCESS TIMBER SALE

Ms. Sexton said this sale is out of the Helena Unit about 26 miles northwest of Helena off Highway 279. It is a salvage sale for 1 million board feet. It includes 194 acres and very little new road construction will be required. We've had public involvement and the issues and mitigations were for big game and silviculture and for access.

606-8            MAIDEN PEAK TIMBER SALE

Ms. Sexton said this proposed sale is out of the Lewistown Unit, 20 miles northeast of Lewistown in Fergus County. This is for 1.2 million board feet, 135 acres. This was done in conjunction with the BLM/DNRC as a cooperative effort. The EA was created in conjunction with the Judith Moccasin Landscape Analysis Project. The department tiered off the efforts done by the BLM. The landscape analysis has been incorporated in a FONSI (Finding of No Significant Impact), the decision was signed by the BLM and the DNRC.

606-9            ALKALI TIMBER SALE

Ms. Sexton said this proposed sale is out of our Stillwater Unit office approximately 2.5 air miles from Eureka. This is for 1,220 million board feet from 204 acres. No old growth will be harvested. Approximately .3 miles of new road construction is required and 6.2 miles of maintenance and minor reconstruction is required. Approximately 3.1 miles of existing road would be abandoned and covered with slash and debris. Public involvement was solicited and issues identified in the Old Highway EA were analyzed. Issues of concern were fuels reduction, noxious weeds, transportation systems and wildlife loss of cover.

606-10           CROWN BUTTE TIMBER SALE

Ms. Sexton said this proposed sale this is located near Belt 6 miles southwest of the Sluice Box State Park. The volume is 1.4 million board feet from 65 acres, most of which will be thinned. There will be a final segment of road constructed across private property. Issues and mitigations are for big game.

606-11           TOOMEY TWO TIMBER SALE

Ms. Sexton said this sale is proposed near Dillon 15 air miles northeast of Wisdom. It has a volume of 790 thousand board feet from six harvest units from 106 acres. The issues include elk range and illegal ATV use. Upon completion of the sale new roads and reconstruction will be physically closed. Weeds were an issue in this smaller sale.

Ms. Sexton said there are five proposed timber sales amounting to 5.6 million board feet.

Motion was made by Ms. McCulloch to approve the five sales. Seconded by Mr. McGrath. Motion carried unanimously.

606-12           SUBMERGED LOGS TITLE ACTION

Ms. Sexton said some background information is the State of Montana owns the bed of Flathead Lake outside of the Confederated Salish and Kootenai Tribal lands. Recently the department received from North Shore Development a request to begin salvage of sunken logs resting in the bed of Somers Bay in Flathead Lake. Ms. Sexton handed out information from North Shore Development. She said once DNRC learned of the attempted salvage operation it requested that North Shore cease operations until it obtained authorization from the department to do so. It is within the department's jurisdiction to have oversight over all lake and river beds in Montana. North Shore claims title to these logs by virtue of a series of assignments. There is included within this action a description of the series of assignments from

MINUTES  
June 19, 2006  
Page 12

Somers Log Company and the Great Northern Lumber Company. It is believed that these logs have rested upon the bed of Flathead Lake between 40 – 100 years. The department's reviewed of these circumstances has generated several legal questions: who owns the unbranded or wild logs on the bed of navigable waters? Who owns the branded logs? And are the logs which have rested on the bed of Flathead Lake for more than 40 years presumptively abandoned? Does North Shore Development have a clear chain of title to the subject logs? We believe the State of Montana does own the wild logs citing a Washington Supreme Court decision. The Washington Supreme Court basically states ownership of submerged logs in the state's ownership of the beds of navigable waters. The North Shore Development may have claim to the branded logs, and believe they have not been legally abandoned. But we have not found any case law that specifically addresses abandoned logs. Actually for personal property it is considered abandoned after five years and for water rights as another example, it is after 40 years of non-use. If these logs have rested in the lake bed for more than 40 years the state is then presuming they have been legally abandoned and they belong to the State of Montana because the state is the owner of the property for which there is no other owner. In order to do this, the department is asking to determine the ownership and she recommends the Board authorize the filing of a civil action for declaratory judgment and quiet title for the submerged logs on the bed of Flathead Lake. We have had other requests for developing the submerged logs and we believe given the substantial request from North Shore Development and other inquiries we've had that this would help settle the issue. Idaho does have a program, as well as Washington's program. Often with these logs about 50% of them are cull logs and we don't have any real accurate indications of what might be resting on the bottom of the lake but it is believed as these companies did ship logs down the rivers and into the lake that up to 20% sometimes 30% of them did sink to the bottom. So there could be a substantial number not only in Flathead Lake but in other lakes in western Montana. The department believes there is an opportunity for substantial income from these salvaged logs. We would like to clarify the issue at this point by requesting authorization of the filing of civil action for declaratory judgment and quiet title in the submerged logs in Flathead Lake. The Complaint for Declaratory Judgment and Quiet Title is included in the Board's packet. And there is information from North Shore Development Company who has been working with the department. We informed them we would bring this issue to the Board because we felt the issue of the actual title, particularly of the branded logs but also as well the wild logs, needed to be settled in a clear and concise manner.

Randy Ogle, Attorney and Co-counsel for North Shore Development Company, said I am co-counsel along with David Zabel, an attorney from Connecticut. Mr. Zabel has traveled here from Bridgeport to be here today for this hearing and I ask your permission to allow Mr. Zabel to address the Board.

David Zabel, Attorney, said in case you're curious about how I arrived here, North Shore Development LLC was a Montana LLC. The principal owner is Donetta DeVoe she is the widow of George DeVoe who with his brother Ronald owned the mill that burned down in the 1950's that relate to these logs. Donetta is here today also and is prepared to address the Board. The other members of the LLC are Steve DeVoe, a nephew, Kim Hansen, and Alan Leener who happens to be my connection. Alan met Donetta in the 1960's when he was traveling as a clothing representative after the mill burned down and she asked Alan to help her get this project off the ground and Alan came to me about a year and a half ago with an offer I couldn't refuse in which he said I really need your help in this. We've got this lovely lady in Montana who has some logs but I can't afford to pay you until the project is successful. So, through a series of events I come here today to address these issues. In connection with these log recovery efforts we did first apply last year and received a permit from the Department of Environmental Quality (DEQ), which was the permit we understood was required at the time to begin these recovery operations. We pulled out some sample logs and that's when the Montana Department of Natural Resources and Conservation became involved and said they thought they had jurisdiction and would require a land use

license in order to continue operations. Since then we have been in communications with DNRC to try to address these issues. The ownership issue that has been raised here I believe is not one that is really an issue. The statute that was cited by the attorney for the DNRC, the Montana Abandoned Property Statute, does not apply in this case and there is a Montana Supreme Court case that says that. That Abandoned Property Statute which talks about property being presumed abandoned after five years doesn't apply because property as defined in that statute is defined to include only various types of intangible property such as stocks and bonds, or tangible property in a safe deposit box. So, when that issue came up in a different context, not with abandoned logs but in a case which involved property of a prisoner that was claimed to be abandoned, the Montana Supreme Court held that that statute doesn't apply to tangible personal property like logs. Secondly, the Washington case that is cited, Tortorelli, we also believe doesn't apply in this case. Tortorelli was a case that dealt with Lake Washington in Washington State and what that court held was that by virtue of the equal footing doctrine and a submerged land fact, forests that had been submerged in Lake Washington, that is standing trees etc., were natural resources of the state that were owned by the state. Also at issue in that case were stray logs that had been cut at some point in time by the Corps of Engineers and what the court in the Tortorelli case said is we are not relying on the equal footing doctrine because we don't believe those are natural resources because they are already-cut logs but there is a specific statute in Washington that says the state owns logs that are cut and are submerged in the lakes. So the Washington case that has been cited by the DNRC does not apply in this situation where we have a private owner of logs with a good chain of title that goes back to the early 1950's that shows that now North Shore Development LLC is the owner of these logs.

Let me describe how that chain of title came about. Back in the early 1900's Charles DeVoe who was George and Ronald DeVoe's father came to work for a company that was established by the Great Northern Railway to do timber operations in Somers. He lived there with his family including George, who was Donetta's husband, and Ronald and he worked for those companies until 1947 or 1948 when the Great Northern Railway decided to stop its logging operations and sell them to private parties. The Great Northern Railway did that through a transaction that went to Alex Schulman Company. At that time, Charles DeVoe came to his sons George and Ronald and said you have an opportunity as my sons to buy the logging operations that exists here that allows you to stay and work in the state. And the title documents for that transfer include not only the property and some of the buildings that were relevant to the logging operations and the sawmill but also title to the deadheads, the sunken logs, in Flathead Lake. In fact this past weekend Ms. DeVoe delivered to me and found an original closing book that has those title documents, including a bill of sale from Alex Schulman Company which was the company that was set up or through which North Shore disposed of its property in the Somers Bay area to these deadheads in Flathead Lake. The Alex Schulman Company sold the logs including the sawmill operations to something called Somers Water Company because at that point in time there was a company town there. The Somers Water Company in turn sold those sawmill operations to DeVoe Lumber Company. DeVoe Lumber Company operated the sawmill and the logging operations from the early 1950's until unfortunately there was a fire in 1957 that burned down the mill. The DeVoe's unfortunately, didn't have insurance and they were almost ruined by that event. What they did do after the mill burned down is they transferred to a company they set up to dispose of the land they owned and the equipment they owned in the area. That company was called North Shore Development Company, a Montana corporation owned by George and Ronald. They had the foresight at that time to transfer from DeVoe Lumber Company to North Shore Development Company title to these deadheads in Flathead Lake and that is one of the documents we've submitted today to the Board. There is a bill of sale from 1959 that transfers title. Over the years North Shore Development Company tried to periodically recover some of these logs. George did it through various individual people and in fact, in the 1970's there was a more formal operation with a local gentleman named Ken Bailey where North Shore entered into a contract with Ken Bailey, they applied to the State of Montana at that time for the environmental permits that were necessary. They got

the permits to raise the logs and there was an operation that brought up about one million board feet. At least in the mid-1970's the State of Montana acknowledged and recognized North Shore Development Company as the owner of these logs. Since that time, because of the economics in the lumber business and the fact that the technology did not exist to locate logs as easily as it does now, now you have side-scan sonar and other devices that allow boats on the lake without disturbing things to go out and actually locate where the logs are and find them to pull them up. It has now become economically viable to have these logs located, raised to the surface, brought to the land, dried out and sold as valuable timber. If the Board has any questions about those economics and about why there was this delay between the mid-1970's and now and what the prices of timber were, we have with us today a man named Greg Bassler from Northwest Management who is a timber consultant that North Shore has retained to assist in these operations. The one aspect of title that the DNRC is relying on to claim these logs are abandoned I suppose is Montana law because there is no statute and the Washington case doesn't apply. We've presented to the Board what the law is about abandonment in Montana. What abandonment requires in Montana is an intent to abandon the logs and relinquishment of possession. Further, under Montana law even if property is abandoned at some point it can be reclaimed by the rightful owner. In this case, we claim and we believe the evidence does support this, in fact, it is the only evidence here, there was never an intent to abandon these logs. If the Board has questions about that, Ms. DeVoe has been involved in these operations since her husband was the owner of the mill in the 1950's, she is here and she can tell the Board what happened over the years, how they came to try to recover these logs at period of times, how her husband, after the mill burned down, didn't have the money independently to fund the significant operations that are required, or at least were required back then to raise these logs. Now you can do it by way of things that are less substantially less expensive such as divers and you don't need heavy equipment to do it any more. We believe we have established to the satisfaction of the Board and the DNRC that there is a good chain of title to the logs, they were never abandoned, and in fact if they were ever assumed they were abandoned at some point they have been reclaimed. What North Shore has done since it was formed is to go out on the lake with a side scan sonar to map where these logs are and we now know where our logs are. We are ready to begin the recovery operations, we don't think we should be put through the delay of a declaratory judgment hearing and we don't think that would be appropriate or necessary. When the DNRC came to us we were willing to talk even though we were the owner of the logs and we believed that would be established and if that were established then nothing would be due to the state by way of a royalty fee. We even proposed to pay a small royalty fee to avoid the further delay that would be caused in this because Ms. DeVoe isn't getting any younger and this project has consumed almost two years of a number of people's lives. We believe the appropriate thing for the Board to do is not to authorize a declaratory judgment action when we think we have established through our submissions that we have both a good chain of title and legal authority in Montana to support our claim of ownership. It would be appropriate to proceed to go through the process of granting a land use license through the environmental assessment that is necessary and allow us to get back out on the lake and get the project going.

Mr. Morrison said do you acknowledge that the bed of Flathead Lake is public property?

Mr. Zabel said I believe that is the case, yes. I don't believe there is a dispute that the bed of Flathead Lake is public property.

Mr. Morrison said so when we address these abandonment issues the question is the same as if your logs were sitting on school trust land, or sitting in a state park, or FWP's land or any other state-owned land whether it was under water or not the issue of abandonment would be the same.

Mr. Zabel said I believe so. In fact, the case we cited in our submissions involved property of a prisoner that was alleged to have been abandoned in a prison which is certainly state property. The principles are the same no matter where the property is.

Mr. Morrison said how important is the branding of the logs?

Mr. Zabel said I don't believe the branding of the logs is important. I believe we have a chain of title from all of the people who were conducting the logging operations in the area including the DeVoe Lumber Company. The logs were brought down to the lake, they were brought in booms and they were brought to the mill at Somers and they were milled there. So our chain of title from Great Northern Railway establishes that we are the owners of the logs whether they were branded or unbranded. Ms. DeVoe can speak to one of the issues on that because while the DeVoe Lumber Company was operating in the area for a long period of time they were the only mill there so there was no need to brand the logs because the logs were being brought down and they were going to one mill. There wasn't any other mills where you would have to separate the logs and establish the brand, they were the only mill that was buying logs in the area and purchasing them.

Mr. Morrison said is it your position that as long as there is a chain of title that the logs of the private party that are sitting on state property unbranded are never abandoned, that they remain subject to that private party's reclaiming them at any time in the future?

Mr. Zabel said no, not that they were never abandoned. If it is established that there was an intent to abandon the logs then that would be the state's burden in this case to establish the intent to abandon the logs, then the logs would be abandoned. For example, if there hadn't been efforts to recover these logs and chain of title, the DeVoe's did what they thought was necessary to preserve their rights to the logs. Not to abandon them. If there weren't that type of activities we have here there might very well be a good claim of abandonment that could be established. But here, I don't think that could happen because the DeVoe's did what they thought was necessary to preserve their chain of title and their ownership rights on these logs and they didn't just leave them lying anywhere on state land. They knew they were in the lake, they weren't going anywhere. There wasn't an economic way to recover them. The technology didn't exist, they didn't have the money to hire heavy equipment. But they knew the logs were there and they passed the chain of title hoping technology would process to the point where they could feasibility be recovered.

Mr. Morrison said if there is a chain of title and you put your logs on our land and you leave them there, they are subject to reacquisition by you and if we want them off our land then its up to us to get them off our land. If we are hosting your logs for 40-50 years, you're saying that's a decision the state made.

Mr. Zabel said the state has certainly allowed those logs to remain there for that period of time. If the state had done something to assert ownership rights over the logs prior to this then it would have been incumbent upon the DeVoe's to come in and say these are our logs, we'll take them, you're not allowed to have them. But the state has not ever asserted ownership rights over these logs until right now. In fact, in the 1970's the state recognized that North Shore Development Company owned the logs. The DEQ recognized that last fall when we applied for a permit again. I believe the state has in fact recognized that North Shore is the proper owner of the logs previously.

Mr. Morrison said if the state files this motion to quiet title wouldn't that be a simple fairly quick way for you to establish your position as a matter of legal record and then go forward based on that? Wouldn't your investments in the rescue of these logs be more secure?

Mr. Zabel said no, our investment is secured by the chain of title we have which is as good as I think anything can exist. If some other party comes in and tries to take the logs, we'll defend those rights. We believe we have a good chain of title and for the state to put North Shore Development through the expense of a declaratory judgment action when we've given the state all of the information, we've shared with the state all of the information we have which shows we have title to the logs. We've given the state all of the documents which show we have good title. What the state stands to lose in this if it decides to go forward with this course of legal action is (1) it loses North Shore's willingness to voluntarily provide a royalty to the State of Montana relating to the logs that are recovered which would go into the state's education fund, we've offered to do that to avoid the delay; and (2) under applicable Montana law this is a case Mr. Ogle told me about, Board of Trustees of Indiana University v. Buxbaum, the state would also be potentially liable for our legal fees in that declaratory judgment action because we've put forth the information that would establish and that a court would find establishes our title. If we're put to the expense of defending a declaratory judgment action and I believe we will win at the end of the day, we would be entitled to ask for our legal fees to be reimbursed in connection with that action. I don't think any of that is necessary. We've provided to the state everything its asked for to show Ms. DeVoe has title to the logs and the LLC she has now formed and is the principal owner of.

Donetta DeVoe, North Shore Development, said we've never had it out of our mind and George and Ron over the years have got into other careers and also tried to find someone who had the money. We had a couple of different people who thought it would be the most dramatic thing they could do to come up to Flathead Lake and drag those logs out. They got up here and found out how much money and work it took and it fizzled out. A couple of years ago my brother was looking for something, he's in the logging business and ships wholesale logs, and he wanted to do it and he had the money. He came over with underwater cameras and began taking pictures of those logs. We were all excited and he knew how they were going to come out, he knew how to dredge. But he got sick and passed away. So there we are in limbo again. Then Alan and my husband talked about those logs since 1960-something and were going to find a way some day. Everybody knows that George and Ron bought those deadheads, kept them in one place after the mill burned. It just never occurred to me to say they were abandoned.

Mr. Zabel said I don't have anything else to add unless the Board would like to hear about any of the economic issues from our consultant, Mr. Bassler.

Ms. Sexton said there are three issues I'd like to briefly address. One, we have reviewed the chain of title and we have found questions, they are spelled out within the declaratory judgment. We feel the chain of title is not clear and there are questions. Two, we do have a copy of the letter of the proposal that was given to us, we discussed internally the offer made by North Shore Development and it amounted to \$2.68/MBF. The going rate for this in Idaho is between \$50 - \$85/MBF. Three, we do have complete competing proposals. Not only for these logs but there are other logs that have had proposals as well. For those three reasons is why the department believes it should be settled in a clear and concise manner and declaratory judgment and quiet title is the reasonable way to go in order to clear the issues.

Governor Schweitzer said as a matter of clarification on historical context, for many years the Stillwater Forest management technique consisted of this: we cut the logs in the winter and we drug them out on the river while the river was frozen, then when the river thawed those logs were sent down to Flathead Lake where they were branded. Unfortunately there were a large number of immigrants and their first job was to ride those logs as they came down the river. I owned a ranch for about three miles along the Stillwater River and there are a lot of unmarked graves along there because of these folks who rode the logs and didn't make it all the way. There were many sawmills around Flathead Lake. When they arrived



on the lake there were folks who sorted them like sorting cattle through pens and took them to many of these sawmills. So in fact, the decision that is made here may well affect a whole lot more and it wouldn't be just this decision we're making.

Mr. Zabel said the offer that was made of \$2.68 was for the branded logs. But the offer was \$12.58 for the unbranded logs, recognizing there is a difference for those things.

Ms. McCulloch said we're under mandate by the Supreme Court for fair market value for State of Montana rental properties, cabin leases, all sorts of things and of course that goes to benefit the school kids of Montana. My question is, has there been any thought to, 40 years of storing logs on our land, has there been any thoughts on storage fees over a period of 40 years would be for that?

Tim Hall, DNRC Chief Legal Counsel, said that's a very good question, I don't know if it has been explored but it would be a reasonable thing to bring out in these discussions. The way we look at this lawsuit is it is a way to discover early on who has title. Even assuming, which we do not concede there is a clear chain of title, I liken this to water rights. You can have a clear chain of title to a water right that was abandoned 60 years ago and it doesn't do you any good to have that chain of title if a court determines it has been abandoned. We're going through a state-wide adjudication process on water rights and one of the big issues there is are water rights abandoned. As you know, people fight over water rights in this state. If we have a state Supreme Court and law that says water rights can be abandoned by non-use I think that can certainly be applied to sunken logs, branded or unbranded. There is a Supreme Court case that was 40 years, the Supreme Court has also ruled about 23 years, if you haven't used water rights. The Water Court itself, although it was appealed to the Supreme Court, ruled that 14 years of non-use raised a rebuttable presumption of abandonment. So the intent to abandon comes from, in the case of water rights, not using them. We think this area of law is unusual, we don't have any Montana cases on point. The argument would be that the logs were not retrieved they were abandoned. The title passed to the state and we have to get the fair market value and storage would be another issue even if not abandoned.

Governor Schweitzer said I think Ms. McCulloch makes a good point. We, as a Board, are always viewed by groups across Montana whether we have protected the interests of the State of Montana. Not being an attorney, certainly not a judge, this is not a legal panel I guess I am of the opinion this is something to be decided in the courts not by us.

Mr. Morrison said it seems to me that the reason why we have to move forward with the quiet title action is because there are a couple of legal issues that are subject to disagreement between the department and the DeVoe's. It is not about whether this is worth \$2 or \$50, or whether there are other examples out there. Those are what motivate us. But question one is whether there is a chain of title, and question two is if so, whether there is abandonment. Those are issues that apparently are disagreed upon and they have to get resolved. Our job as the Land Board is to represent the trust with our primary loyalty and in this case it probably means having a court sort those two issues out.

Mr. Zabel said I understand and appreciate what you said and I thank you for listening to me this morning.

Governor Schweitzer said I for one would be anxious to watch those beautiful larch trees from a long time ago come back to the surface and be used in building some beautiful homes in Montana.

Mr. Johnson said for my own edification, the director talked about the fact that there were competing bids now. Was there any activity on the part of the department with regard to salvage or processing these deadheads prior to North Shore's activity?

Ms. Sexton said as far as I know we have gotten proposals but we have not had any direct activity.

Mr. Groeschl said we've had, in February 2006, a request for a permit to salvage sunken logs off the bottom of Flathead Lake from a gentleman in Idaho, Mr. Jim Tracey. As well as North Shore submitted a proposal to salvage logs off of Flathead Lake. So, we've had two competing proposals to salvage logs off of Flathead Lake. The first request in February did not claim ownership of those logs, basically looking to have a permit to salvage the logs and would pay the state a fee per thousand board feet that they salvaged. Whereas the DeVoe's have claimed ownership of the branded logs. There is some competing interest for those logs. Again, in February we had a proposal from Idaho as well as the proposal from North Shore Development.

Mr. Johnson asked if North Shore's proposal was in place first?

Mr. Groeschl said actually, the gentleman from Idaho, Mr. Tracey, came in first.

Mr. Johnson said and that was unsolicited?

Mr. Groeschl said yes, it was unsolicited.

Mr. Zabel said North Shore's proposal was made last fall when we made an application to the DEQ to get a permit to do this. So we applied for and received a permit last September from the DEQ for this project. It was only when the DNRC got involved when we pulled some sample logs that these other issues were brought up. So our project proposal was made last fall.

Motion was made by Mr. McGrath to adopt 606-12 as recommended and authorize the staff to file a quiet title action as proposed. Obviously there are lots of facts in dispute in this situation. Perhaps even some issues of law that need to be resolved. We don't sit as a court of law. This is precisely the reason that courts of law exist and this is the kind of dispute that should be resolved in the court system. Seconded by Ms. McCulloch. Motion carried unanimously.

606-13      COMMUNITIZATION AGREEMENT(S)

Ms. Sexton said we have four communitization agreements and I can go through them and take them as a package if the Board agrees.

A.      WYOMING RESOURCES CORP

This is Roosevelt County and is an agreement to communitize state-owned acreage in a permit development in conformity with regulations of the Montana Board of Oil and Gas Conservation. With Wyoming Resources Corporation, this is for 25% communitized area, the department owns 80 acres within 320-acre spacing unit.

B. BURLINGTON RESOURCES

This is in the horizontal Bakken formation in Richland County. This is a 25% communitized area, the spacing unit is 1280 and the department owns 320 acres within this area.

C. QUICKSLIVER RESOURCES

This is located in Toole County and is a 50% communitized area, and is a Swift formation gas well. The spacing unit is 160 and the state owns 80 acres within this area.

D. DEVON ENERGY CORPORATION

This is in Blaine County and is in the Eagle Sand formation. It is a communitization of 68.75%. The state owns 440 acres out of the 640 mineral acres in this spacing unit.

Ms. Sexton recommended the state receive its proper share of production from these units and recommend approval of these communitization agreements.

Motion was made by Mr. Morrison to approve the four communitization requests. Seconded by Mr. Johnson. Motion carried unanimously.

INFORMATIONAL ITEMS

606-14 DNRC FISH PASSAGE ASSESSMENT PROJECT  
(power point presentation)

Ms. Sexton said we have a presentation today by Jim Bower, the department's fisheries biologist. This is a quick overview of the efforts we are making in fish passage. This project began several years ago to address stewardship, long term planning and the resource management plans we have on the ground. Structures are in place but they are not as fish-passage friendly as they might be so we want to mitigate these issues on our roadbed crossings and set up a long term approach as to how we are going to deal with these issues. Jim has done an excellent job of putting together a brief program on this issue.

Jim Bower, DNRC Fisheries Program Specialist, said I'm here to give you a short presentation on the DNRC fish passage assessment project. I've been with DNRC for a little over three years and have been in the field of fisheries and timber management for nine years. This informational presentation discusses the concept of fish passage on state trust lands. For the purposes of this presentation I would like to take a few moments to make sure everyone understands what is meant by fish passage. The first idea of fish passage that needs to be understood is that fish migrate. Most people think of salmon when they hear of fish migration. The same biological processes of migration occur with virtually all species of fish that inhabit the rivers and streams of Montana. More specifically what we are talking about is the behavior of fish migrating up and down the different streams and watersheds in order to seek new habitats for spawning and over-wintering, to seek new or seasonal food sources, or to avoid adverse stream flows or adverse stream temperatures. The second idea of fish passage that needs to be understood is that certain types of road-stream crossings such as culverts or old bridges that were built using trees and excavating material and some fords can impact important fish populations by limiting fish passage. If a fish is unable to pass through a road-stream crossing it limits migration behavior and access to available habitat. When you are talking about fish passage you are talking about the ability of fish to migrate up and down the

streams through different types of road-stream crossings. Some important points here of limiting fish passage can have a significant, adverse affect on native fisheries such as Westslope cutthroat trout and bull trout. Limiting fish passage can also adversely impact non-native but otherwise important fisheries such as rainbow trout and brown trout. We are all aware of the value of fisheries throughout this state as this natural resource is an important component of local recreation and tourism. What we are getting at with this particular project is an inventory and assessment of the existing levels of fish passage on state trust lands. Especially those road-stream crossings that are considered part of our inheritance or legacy road systems. We are identifying restoration needs for improved fish passage. Some culverts prevent fish passage because of the outflow jump which is a barrier to most adults. If an adult were able to negotiate the outflow jump and make it into the culvert the combined water velocity and gradient within the culvert far exceed the swim capabilities of these adult native fish. The next slide provides another example of another road-stream crossing but this structure allows the passage of native trout. In this case this culvert in the Sula State Forest was reinstalled as part of restoration efforts after the Sula fires of 2000. The reason this culvert allows fish passage is because the culvert was designed to be installed below the normal stream grade and this facilitates the development of normal channel substrates, flow velocities, and other stream features within the culvert.

What are the main reasons for conducting this project? The first one is for trust land stewardship. In addition to providing income for the school trust we are responsible for maintaining the long term biodiversity of trust lands through good land stewardship. In this regard, DNRC is not responsible for managing fish populations, such as the role of FWP. But DNRC is responsible for and takes great pride in managing for diverse and healthy fish habitats on trust lands. Long term financial planning is another reason we conducted this project. By conducting the inventory now we know exactly where we have problem sites which gives us the ability to capitalize on grant opportunities as they become available as well as other potential inter-agency water quality or TMDL funds. The information also allows for more informed strategic planning when working with forest management activities. Especially when roads need to be brought up to Best Management Practices, or BMPs, under timber sale contracts. DNRC is also a contributor to several inter-agency resource management plans. Among these cooperative plans are the Montana Cutthroat Conservation Agreement and MOU and the Montana Restoration Plan for Bull trout. Both the plans promote enhanced fish passage as restoration goals. Project details include inventorying all road-stream crossings on state trust lands that intersect both known and suspected fish-bearing streams. The project was initiated in 2003 and completed within budget and on schedule in 2005.

Mr. Bowers presented some of the project results. He showed the general project area and all the inventoried road-stream crossings. Red and black marks depict the fish passage sites on state trust lands. The red marks display the locations for fish passage that are either not impaired or not a maintenance issue for DNRC. The black marks show the locations where fish passage has been determined to be both impaired and a long term DNRC maintenance responsibility. The total number of road-stream crossing sites that were inventoried during the project is 875, approximately 775 sites were determined to be sites where fish passage is not an issue for long term DNRC management. These were the sites with the red marks. These 775 sites were determined to not have fish passage issues for a multitude of issues such as the site already allowing fish passage or the structure no longer exists, or DNRC does not have jurisdictional control of the road-stream crossing. Of the 875 inventories approximately 100 locations were determined to both impair fish passage and be a long term DNRC management responsibilities. These were in the western part of the state.

Where do we go from here? What are we planning to do with this information? First off, we have a tentative target for restoring fish passage where appropriate by bringing all the sites with known impacts to fish passage up to BMPs within 30 years. This is equal to restoring fish passage at approximately three

road-stream crossing sites per year on state trust lands. In terms of restoring fish passage, we have typically talked about replacing culverts or bridges, upgrading the stream channels at some sites, or even removing crossing structures entirely until they are needed again in the future. When designing these structures for restoration of fish passage we will have to consider quite a few variables such as stream flow, stream size, engineering constraints, and of course financial constraints. The fish passage restorations will also be prioritized based on a broad coarse filter using variables such as species status, species genetics, and existing levels of fish passage impairment. For example, fish passage sites with bull trout, the federally listed species, will be analyzed for restoration before sites with other cold water species. Fish passage sites with genetically-pure Westslope cutthroat trout will be analyzed for restoration before those sites having hybridized populations.

As most of you know, the Forest Management Bureau is in the process of developing a Habitat Conservation Plan for forested state trust lands. Bull trout, Westslope cutthroat trout, and Columbia River red band trout are the three aquatic species proposed for coverage under the Plan. The thirty year timeframe and prioritization schedule described are consistent with the conservation strategies for fish passage that are in the proposed HCP. The information will also allow for the current and future coarse collaboration with other landowners in different watersheds. For instance, I am currently working on a fish passage subgroup involving DNRC trust lands, the Forest Service, Plum Creek, and FWP where we are working on methods to better prioritize fish passage restoration in watersheds with mixed ownerships. DNRC will be working especially close with FWP to ensure the proposed fish passage restorations are consistent with long term species conservation goals. Not only is this close collaboration better for fisheries population management but there will also be opportunities to lower the long term restoration costs across different ownerships.

A quick review of the potential funding sources for the fish passage restorations include grant opportunities, road maintenance associated with timber sale contracts, and Forest Improvement funds. The future also includes enhanced fisheries stewardship and improved water quality.

## COMMENTS

Mr. Johnson said there have been a number of folks from different quarters that have come to me expressing frustration over the lack of progress with regard to developing the coal at Otter Creek. That is a letter requesting we put the item on the agenda next month. We are currently preparing a letter for the department and the other members of the Board that will detail the aspects of that issue that we would hope the department could speak to at the meeting next month.

Governor Schweitzer said Secretary Johnson I am glad you brought that to our attention. I saw that recently at a Republican event you suggested there are available to us some very real and very exciting technologies in the area of coal and the time has come to do more. I think you also mentioned there is a proposal to build "a" plant to convert coal to liquid fuels which is "a ten year ten billion dollar pipedream built on 70-year old technology." I am glad you brought that before us. I note that about ten months into your stay here on the Board you noted to a local newspaper "its been remarkable non-controversial experience and been nearly all unanimous votes." Furthermore I noticed during 18 meetings I tallied the number of times you've either said the word Otter Creek or coal, and that would be in 18 months nine times. Just for your information, I've used the terms 31 times, Morrison 23, and McGrath six. Its good that you're interested today. We've asked the staff to prepare the work that has been done on Otter Creek during the course of the last several months.

Ms. Sexton said I can give you just a brief overview and then Monte Mason has some other information. In the late 1990's we did receive eleven sections in the Otter Creek project area, the mineral rights to those sections designated specifically for potential coal development. Since that time, the department has completed cultural inventories and extensive coal resources logging and coring program. In fact, the 2003 legislature provided \$300,000 in trust revenue funding to acquire additional data. The current study we have now we are doing in conjunction with Great Northern Properties. These eleven sections are quite interspersed checkerboard with Great Northern Properties so they are an obvious interested partner in our efforts here, so we are doing a joint study with Great Northern Properties. The resulting report will include updated geologic modeling, accessing available resources, coal quality, mineability, strip ratio, and the range of expected mining costs. Expected mining costs in this report will include consideration of transportation by rail either with or without the proposed Tongue River Railroad. We are in the process of completing this report as we have visited with many of our partners who are interested in this. When this report is completed it will be made available to the public and we will actually send it to all of our potential stakeholders for review and feedback so we can assemble, as we have indicated to you, a comprehensive plan for the development of the Otter Creek tracts in the most beneficial manner for the state and particularly for trust lands in the area. So we have moved cautiously but deliberately with this process and we are in the process of completing this report, we will then proceed to distributing the report and have a comprehensive plan which we will bring to the Land Board as to how we might develop this. We want to be very thoughtful and cautious with this so that we have the best possible approach because this is a very large area and we want it to be developed to our benefit, particularly for trust lands interest. I know Monte has some specific information and we also have some other information about coal development in Montana generally.

Governor Schweitzer said Monte, would you start with the slide that gives us a historic perspective of Montana coal production going back all the way to 1890 and bringing us forward to 2000. Its interesting that Mr. Johnson suggested there is some kind of 70 year old technology that is being considered because some of the gentlemen who walked into the room just a moment ago come here from Tulsa, Oklahoma to show us their technology, Syntroleum who is making fuels now and has just received a DoD contract to make the synthetic fuels. Of course that is updated. This is very important. The slide begins at 1890 with Montana's historical coal production. Since this discussion of coal came up at a Republican convention we try to keep things non-partisan here but let's just talk about what happened over the last course of years. Let's start with 1952, that was the last year that Governor Bonner was in office, then we drop to 1960 for eight years of Governor Aronson, then we have flatlanded almost nothing until 1968 when Forrest Anderson was elected Governor. Then things got pretty excited in Montana in terms of coal production. So we went four years with Governor Anderson and we increased 10 – 20 fold and went eight years with Tom Judge. We got a little way up here in 1988 to about 39 million tons with Governor Schwinden. That's what it looks like with 20 years of Democratic governors and coal production, and that what is looked like for the previous sixteen years of Republican. The next slide will show us what is happening the last sixteen years in Wyoming versus Montana. This is 1988, this is an increase in coal production from 1988 to present, you can see we're at 39 – 40 million ton. So from 1988 during the Stephens administration, the Racicot administration, the Martz administration somehow we have flatlined in Montana. The policies we had in Montana allowed us to not increase coal production at all. During the same time our neighbors to the south, Wyoming, went from 150 million ton to 400+ million ton during those sixteen years. So, what we are attempting to do is reverse the trend and go back to those years where we had similar to the Anderson/Judge/Swinden years. We have a lot of coal in Montana and its not all contained in Otter Creek. But let's continue on with what has been going on in Otter Creek during the last year.

Monte Mason, DNRC Minerals Management Bureau Chief, said I can speak briefly to some of the activities targeted where we are focusing on the Otter Creek area. Specifically to Otter Creek, the first slide gives a general project location. To the west you see the eastern edge to the Northern Cheyenne Reservation, you see Custer National Forest which surrounds Otter Creek both to the west and to the east, and right in the center would be the Otter Creek property. Zooming in closer, we see the actual area known as Otter Creek, and what you see there is a checkerboard ownership. Initially there were three lighter blue squares there, the Sections 16 and 36, which are the traditional state lands. The darker blue squares are the 7,600 acres we received from the federal government in a grant of lands in 2002. Together those comprise about 9,500 acres. What is very pertinent to the entire discussion related to Otter Creek is our ownership pattern. Typically we are Section 16s and 36s and are not in the driver's seat as far as what happens with development because there is federal and private land and the state will either have a section or so in any particular development. We see this on the other mines that are in Montana. Here we have a checkerboard ownership with Great Northern Properties so each of us have a 50% share of the potential resource that is at Otter Creek. Before we accepted the Otter Creek tracts we did enter into a settlement agreement with the Northern Cheyenne Tribe. That was an agreement that took care of a potential lawsuit that was discussed between the Tribe and the Land Board. They had alleged there would be some impacts to the Tribe based on the development of Otter Creek and they cited some potential violations of MEPA and FLPMA and the federal government's trust responsibility to the Tribe. In resolving that issue, we reached a settlement agreement between the Tribe and the Land Board that provides for coordination, an operating plan that will be implemented upon leasing, outside what is required by the regulatory requirements by the State of Montana. Including, not quotas or preferences, but meaningful opportunity for hiring and contracting through training, recruitment, workshops, hiring a facilitator, dealing with creating a board between the operator and the Tribe to work through issues. It addresses cultural concerns the Tribe may have where we coordinate with the Tribe and look at mitigation and impacts based on the Tribe's cultural standards. We've been proactive with the Tribe from the beginning. After accepting the lands we embarked upon a process of gathering additional data in order to determine the best way of promoting this and developing a mine and ensuring fair market value for the trust. The statistics are updated and points out what the department has been accomplishing over the last several months. As you know, we've been involved with Norwest out of Salt Lake in cooperation with Great Northern Properties to take a look at the data that is available. The data that is available out there now is more than what anybody has analyzed before. Obviously there is historical data the BLM had acquired over the years; there is also proprietary Great Northern Property data that had not been available for public analysis before. There is also the data the department acquired in 2004, the most recent and detailed data, to further define the coal we have out there. The study that is currently going on and should be ready in a few weeks is a culmination of looking at all that data and coming out with the most detailed data we are able to come up with at this time, which is going to be very useful for companies that may be interested in the development of that coal, what their interest level might be, and what they might be willing to bid on it. The statistics are some of the preliminary data we've gotten out of that. So even in broad terms, we have additional data that can be summarized and presented to folks. The estimate, and this is for both sides of the checkerboard – the state and GNP, we're looking at 1.4 billion tons of recoverable coal. The total school trust share, obviously, is going to be half of that. The historic split of the Otter Creek property has been tract I, II, and III into logical mining units. What we have now are much more detailed looks. We have the potential for six logical mining units depending upon how you group them.

Governor Schweitzer said Secretary Johnson you said you were aggressively pursuing, are you familiar with the contract that has been written between the State of Montana and Great Northern Properties?

Mr. Johnson said yes.

Governor Schweitzer said so, is there any questions you have relative to that in developing this?

Mr. Johnson said not at this time.

Mr. Mason said with the coordination agreement between the state and GNP it basically starts from the ownership pattern. We are both out there and we are in the same position in that we have coal but we don't have a way to get it to a conventional market. We need the Tongue River Railroad Company (TRRC), as that goes hand in hand with the conventional development of the Otter Creek property. But we're both in that same boat, so early on we recognized that working together to coordinate our efforts to secure data, to put information out there, to come up with the selection of an initial logical mining unit for lease; the more we coordinate on that the better off we are as co-owners. Obviously, it does the state no good to lease its tracts if GNP is not yet ready to do that. We're not going to get value for our tracts because no mining can be done, and vice versa. That agreement is in place and it is working well.

Governor Schweitzer said in the area in addition to what the State of Montana owns and GNP, there is other coal in a 20-mile radius in that area?

Mr. Mason said there is. The Otter Creek area obviously is the central area. If you come around the Custer Forest and the Tongue River there is the old MontCo area of proposed development, and there is Bridge Creek that has potential for development as well.

Governor Schweitzer said someone suggested that the first ones to lease before there is any infrastructure is likely to get a very low price in a competitive bid for those leases. And the ones who hold out until there is infrastructure, i.e., railroad, a permitted mine, since there are about four or five different owners in the area, the one who goes first may well get the lowest prices and the prices might go up in the future relative to what has occurred in Wyoming.

Mr. Mason said it is an interesting situation. Somebody needs to go. The two go hand in hand, you have to have a railroad, you have to have a coal mine. They both depend upon one another. But for anybody bidding on coal leases, the earlier you are in the process and the more that there is some risk associated with the development of a railroad, if you don't already have it [the railroad] obviously that plays into what you're willing to bid for coal in order to make an economic project. Mr. Mason said I do have some draft information from our study I can go over briefly. The first information I handed out to you was basically in much more cogent form, some written notes I was looking at as I talked to you here over the last few minutes. It is an updated summary with the visuals that are on the screen and also a larger version of the Otter Creek coal tract map. I'd like to have you look at the second handout, the Table of Contents. This is a draft Table of Contents from the report I was referring to. This is the kind of information we are going to have available for folks that hasn't been available at the level of detail or with the amount of source data that is reflected in other reports. They are much older and they are more general. If you look at the first page, data sources are reviewed, their accuracy and adequacy, methodology for review, geology and modeling results. There is a lot of data now over stratigraphic outcrop zones and structure. There are new resource estimations and they are in much more detail than what we've had previously. Coal quality is the key issue out there. Along with quality modeling including all the new data, there is also a review of the vertical variability of the coal. That has been an issue with potential development because we have high sodium coal. Sodium levels out there even with the additional data we've discovered or gathered and analyzed shows we are going to have 7% - 8% sodium in our coal. High sodium is bad in terms of the boilers that this coal is used for. High sodium in the ash will create slag in the boilers and it creates operational problems. Most of the upper mid-west



markets that use coal from Wyoming, Montana, will opt for the lower sodium coal. However, there are a handful, ten plants or so, that we've identified in the study that are capable of handling higher sodium coal and typically currently they are getting their coal from other mines in Montana, up to about 20 million tons per year. That's Spring Creek, et. al. But those mines are playing out, so there is an opportunity even within the current market, an opportunity we have to get this coal in in the next several years to some of those markets.

Governor Schweitzer said Secretary Johnson said there is available to us some very real and very exciting new technologies in the area of coal and that he is aggressively pursuing them. Given what we know about the Otter Creek coal, would you recommend pulverized coal, the technology fluidized bed, or IGCC? And which of the IGCC's could you choose?

Mr. Johnson said the fact of the matter is, that particular project I referred to would not necessary involve Otter Creek coal at all.

Governor Schweitzer said for the rest of the coal in Montana, would you break it into three major classes of coal and which of these technologies would you choose for each?

Mr. Johnson said Governor I did not come here to debate with you today. I came here to raise an issue that I think needs to be addressed. I am frankly, gratified that you directed the department to respond as quickly to my concerns as you did with the preparation of this report. The fact that it was not on the agenda as an informational item I assume it was created in between my remarks Friday and today. It sets the groundwork for us now, as a Board, in a non-partisan and non-confrontational manner to enter into a dialogue beginning at the next meeting that hopefully will take all of us to the end point we want to reach with regard to developing this incredibly important resource in Montana.

Governor Schweitzer said the point here is there has been an incredible amount of work during the last 18 months and while you only referred to it nine times in 18 meetings, there has been a great deal of work that has been done. Today we are going to go through this so that before you make remarks, and I want to be very clear about this to all of us who serve on this Land Board, it is imperative that Montana pull together to develop our resources in Montana. If we are knowledgeable about what we're saying in public about these resources we can be helpful in attracting new investment in Montana. If we are not knowledgeable, we are not helpful. So the reason we are doing this is so no member of the Land Board or any of their staff says some things that may jeopardize future investment in Montana. So we are going to complete this education process here today. We'll go through these technologies, what we've done with Otter Creek and where we're likely to go. Not only with Otter Creek, but with the rest of the coal resources in Montana.

Mr. Johnson said the fact of the matter is, it is gratifying to know that all of this information has been developed. It has not been shared, at least with this member of the Land Board. And if, in fact, that information was in the possession of the department and of your administration, I think it would have been appropriate for it to have been shared with this Board.

Governor Schweitzer said once again Mr. Secretary we are going to continue. I know your staff has been sharing information on a routine basis with the staff of the Land Board and have been actively involved in the discussions of what we are doing with coal and in particular the Otter Creek tracts. We'll just continue because you requested to do it, we'll do it today.

Mr. Mason said I mentioned the vertical variability of coal and it's importance to folks because of the high sodium levels companies need to know (1) what is the make up of the sodium level across the logical mining unit, and (2) also vertically. That gives them key information regarding what they can do to blend coal to meet certain requirements because in the study we have it shows quite clearly that blending will be needed to meet certain markets. What I've handed out here now just as a example, the first page is a conceptual cross section from north to south across the Otter Creek area. I say conceptual because the report has detailed stratigraphic cross sections across the whole area to show the variability of the coal. What you see here is the coal, the Knoblock seam, is not contiguous throughout the area from north to south. In the central part it is. You have the Knoblock seam. As you go north, it does split out into the Upper Knoblock and Lower. As you go south the Upper Knoblock actually parts again into the upper upper seam and the lower upper seam and of course, the Lower Knoblock. That is a conceptual cross section. The additional data I have attached is just an FYI to show a representative color copy of the kind of data they have analyzed, which is vertical distribution of key characteristics of the coal for each drill hole we have out there. What that allows the consultant to do is come up with these summary tables such as C-1, C-2, and C-3 which are vertical quality analyses of the various seams. It includes and shows pre-2004 data, the 2004 data, and all data combined, creating a higher level of confidence for those people that might be interested in looking at this particular resource. Armed with that, what they are able to do is come up with logical mining units dealing with that kind of coal. The map shows the latest review and the latest thinking on the particular logical mining units that might have potential at Otter Creek. The northern part of that, east of Otter Creek, is LMU-1 (logical mining unit) also with area A-1 attached to it. Below it to the south is LMU-2 which is comprised of two sub-areas, areas A-2 and A-3. To the west of Otter Creek you'll see LMU-3, area B-1 and LMU-4 area B-2. Over on the legend of the map you'll see the stripes in there reflect the consultant's work on developing mine plan proposals at the level that is needed to do mine engineering and mine economics to show what kind of production can be expected; what the over burdens might be, and what the cost might be to develop those. They've taken those logical mining units out 40+ years in developing the resource. The draft spreadsheet attached are the data they have come up with for a particular LMU. The first page would be mine plan volumes for each of the LMUs. Down the left side and across the right on the X axis are year-by-year production volumes. Not only do they show production volumes but over-burden ratios, in-situ volumes, rehandle ratios, factors that a potential party would look at to see what is it we have here and what are the economics and what could be done with this to try to make it a profitable endeavor. The last table is taking that data and developing mine cost models that look at what would it cost to do that; capital, cash or non-cash costs, taxes, everything a company looks at. Obviously, if a company gets more serious, they will look at this closer, they will drill more holes, they are then going to go to a much greater degree of detail. But this gives the best look we've had to date on what we've got out there. Where this could go with us, getting to this point; where we intend in the very near future to be back to the Board because ultimately what this leads to is between Great Northern Properties and the state. We need to look at what CoalMont is doing with the railroad, what we've got, what industry interest is in this, and we need to make a decision on how to best get the optimum value for what is a huge resource, 1.4 billion tons. And that is the next step for us, to get this report finalized and polished. As you look through it you'll see it there is still some errors, things put in twice, etc. We've got some final polishing to do which will be done very shortly. We intent to take that out to industry and everybody and we're going to show it around with everybody we can get hold of and see what the feedback is. When I say "we" this is of great interest to both Great Northern Properties and ourselves. With that then, we're (both GNP and the state) going to have to come back to the Board and say this is what we got, here's what we think. We're going to have to come to a decision on when, how, where, which logical mining unit to go with first. You don't lease the entire area out because there are four areas there that each are capable of supporting a logical mining unit. You want to get one out there first. That's where we are, that's what we have. We are going to be back to you.

Governor Schweitzer said thank you Monte. If any of the staff for the Board members would like a further briefing, you are available to make those briefings in the past or in the future?

Mr. Mason said certainly sir.

Governor Schweitzer said I'd like Jeff Hagener up if I could. There is one glitch. All of the discussion of development of coal requires infrastructure. One of the infrastructures we're talking about is the Tongue River Railroad Company. Jeff, I know you've been working for some time with the TRRC relative to the fish hatchery. If you could give a briefing on where we are, I'd appreciate it.

Jeff Hagener, Director Fish, Wildlife and Parks, said we've been working for essentially 25 years with the Tongue River Railroad Company. It was proposed that long ago and has gone through several reiterations. One of the things with the railroad, the biggest concern we've had with FWP is that the terminus or beginning of the railroad is projected to go right along the edge of our fish hatchery in Miles City. The Miles City fish hatchery reflects about a \$25 million investment we've put in there and it also is the only hatchery throughout the U.S. that is raising disease-free pallid sturgeon, which is on the endangered species list and is very close to extinction. It is a major concern of ours exactly how the railroad crosses by the edge of our property. We've had numerous discussions with them, most recently we did have an information item before our Fish Wildlife and Parks Commission to talk about the possible easement that would go across the hatchery. I do have copies of the letter I sent to Tongue River Railroad Company after that. Basically we are in the position that ideally the best alternative for us would be to move the railroad away from the hatchery itself. But on the other hand, if the railroad feels it is the best location, as long as the issues we see are mitigated and well protected in the hatchery production we have there, we think we could go ahead with an easement but that has to be approved by our commission and we're still in the process. One of the major concerns we had at the hatchery was simply vibration. Vibration on fish in larval stages and egg stages can be very influential on whether they are reproductive or not and whether they are going to survive. The TRRC has agreed and within the last month, they went out and started some preliminary studies which we asked them to do to measure vibration of what it would be as the railroad goes around the hatchery so we do know what it is and if there is an impact to the fish. The US Fish and Wildlife Service experts with pallid sturgeon recovery are going to do a follow up study to look at those vibration analysis and see if it would in fact affect the pallid sturgeon. That's effectively where we are, we are in the process of working with them. He handed out the letter he mentioned.

Governor Schweitzer said whether we are talking about Otter Creek or any of the other coal resources in Montana, it means development of infrastructure. Probably the setbacks we've had relative to Wyoming over the last 20 years is that they've been in a position where they had a railroad built right into great quantity of their coal, the other thing is they had some of that coal that had a very low overburden to coal ratio. So they had some advantages. We are concerned about infrastructure so we've been spending a good deal of time on pipeline transmission work. If we could go to that now. You can't move coal out of Montana and you can't sell it unless you've got rail or unless you've got pipelines in terms of liquids or unless you've got transmission lines. Dozens of coal companies, technology companies and financial companies have been to Montana and when they come we show them this overlay of Montana's coal deposits relative to where we have infrastructure: pipelines, transmission lines, etc.

Evan Barrett, Governor's Office of Economic Opportunity, said whether it be Otter Creek or other coal that we own or general coal in Montana the infrastructure is an important thing. There are many possible projects in Montana, Otter Creek is only one of them. The business decisions that need to be made are often driven by the presence of the infrastructure, the highways, railroads, transmission lines, pipelines,

and of course juxtaposing those to the location of the coal. I'll hit on some potential transmission projects for Montana. First would be the Northern Lights. Of course, right now what Montana has done, especially when you look at this period of flat growth, is we are just simply moving coal. We're not moving electrons. There are two ways to make advantage of our coal presence in Montana and moving coal out on railcars is just one version of it. In fact, the moving of electrons provides the opportunity to produce better jobs and a better tax base by the presence of the plants it would take to do that. Subject to the transmission lines. The first would be the Northern Lights and that is high voltage direct current line. The Northern Lights project is a line that originally was going to come out of Canada, but now this line is designed to start in Montana, probably in Townsend, with a feeder lines from the eastern coal fields feeding in here and a direct current line down to Las Vegas. Linking from there longer term into Los Angeles and into the Phoenix and the southwest area. This is a loop that should complete the circuit. This kind of a line is well advanced. He showed a slide depicting a comparison between normal transmission lines that are grid lines moving about 3,000-4,000 mega watts of power and what a DC corridor looks like delivering 3,000 mega watts of power. This is an advanced technology. It has certain constraints upon it but it is a good technology. This particular line is soon to be submitted to the BLM for the initial permitting that will come into place which will then be followed with DEQ playing our role in the permitting.

I want to mention our participation in the Frontier Transmission Line. The Frontier Transmission Line is a line that is basically used to do more connections into California through Nevada, Wyoming, and Utah. Montana and Idaho have been working with the principals of this line and the other states to get the northern end hooked in. Actually you may have heard of the Frontier Line and probably the Northern Lights project will become integrated with the Frontier Line or in fact happen in front of it and the Frontier Line will piggyback on top of the Northern Lights project.

I want to mention the Montana-Alberta tie line. This particular line comes from Alberta down into Great Falls. It is not a long line but it does an awful lot. It does two things, one is to gather. Because alternative energy is another important element of our moving of electrons in a balanced portfolio to the 600-pound gorilla market in California which is looking for renewables as part of the portfolio. This is particularly helpful in moving wind power. In addition to that, this is a big time project about increasing the reliability and stability and competition into markets. Right now we have some difficulty moving electrons out of Montana and this will help stabilize some of those sources. In addition, we are working with BLM, which is the lead agency in the energy policy act which calls for, in Section 368, the creation of the selection of corridors for public land, Section 2-1221 is for private corridors. There are public corridor issues in western Montana. As we get into Section 1221 there will be more activity in establishing a corridor but we are working with BLM in terms of identifying the corridors for getting outside of Montana for future transmission development. Those same corridors can be used for pipelines as well. The Rocky Mountain Area Transmission Study (RMATS) which we've been working with since we got here shows the outlook for the Rocky Mountain area. Based on that study most of the movement inside the state is projected east-west movement and not north-south movement because the markets, the south markets, are outside of the area.. The broader look from the outside is that when you look at it there is a major corridor, Northern Lights has identified it and its predominantly on federal land, so we can take the Montana product and move it through these corridors that are north-south. Not only will we do the east-west, but we will do the north-south movement under the RMATS analysis and we are proceeding in those veins. As a point of reference, all of these transmission projects are now under review at DEQ. The last one has just been completed. But there is a whole series of these that relate to the interconnecting east-west. To the east end with WAPA and to the west with BPA. Of course, we also have the Northern Lights and the RMATS that take us on the north-south route which is not identified in here yet because those projects will be coming forward after the Northern Lights project has been advanced.

He showed a map of the pipelines and transmission lines in relationship to the energy resources. You can see the different kinds of coal. The lighter is lignite and the medium colored is sub-bituminous coal. The bituminous coal in the darker color. The juxtaposition of the coal mine opportunities is Otter Creek. Right now its biggest challenge is the lack of infrastructure to support the development, among others including making sure that constitutionally we get the right price for it. The lack of infrastructure affects the price. If you're going to buy coal and you have no means for delivering it, you will pay less for it than if you got the delivery mechanism in place or at least laid out planned and financed. Then the value of the coal goes up.

Governor Schweitzer said earlier on I asked the question what would you choose? Pulverized coal, fluidized bed, IGCC. It depends upon where your market is to begin with. Just last week I was with Governor Schwarzenegger and they were anxious to buy 20,000 mega watts of electricity and more but they will only buy coal if it is Integrated Gas Combined Cycle (IGCC). They won't accept PC, they won't accept fluidized bed. Unless we are able to sequester the carbon dioxide and blend it with so-called other green power like wind, we are not going to be in the market of selling electrons to California. So, if in fact we are going to IGCC, that will be one of the directions we go because California has such a large market, then we have to slice and dice which of these coal fields are we developing because there are contrary to some suggest 70-year old technology, technologies that are evolving right now companies with patents that favor one kind of coal over another. For example, the GE technology is one that favors bituminous coal. We have a very small quantity of bituminous coal. The Shell technology is coal neutral but it is expensive technology to get that neutrality. The Kellogg Brown and Root and Southern Company has developed a technology that is very good for so-called Powder River Basin coal which should be for the most part sub-bituminous but it is also a technology that would work with Montana's lignite. So, when we are talking about what to develop in Montana as companies come, and there have been dozens that have come here, we gave them a matrix that looks like this, we show them where our pipelines are, we show them where our electricity lines are, we show them what kind of coal we have. So we've spent a great deal of time developing this information so when companies like Syntroleum, who is here today, come to Montana to ply their new technology with coal we have in Montana, in a very short period of time they can slice and dice and say does my technology work on your kind of coal? Do you have the infrastructure that surrounds a particular coal field? Who owns it? How much? How deep? What strip ratio is. This has taken a fair bit of time putting these resources together but it is imperative if we are going to develop the coal fields in Montana. That, frankly, is what has been lacking for the last 20 years, the ability to go out and sell those resources we have in Montana and be competitive with states like Wyoming. We are becoming competitive because of this kind of work.

Mr. Barrett said I'll mention the types of Montana coal. The first one is bituminous. By and large that's got a high BTU value and low moisture. Those are the two major contributors. We don't have much of that, we have a lot of sub-bituminous and that is where most of our opportunities are going to go for some of the new technology. Albeit some of them are now able to use our lignite as well. In this case you have kind of a medium level of moisture and the BTU content is significantly higher than the lignite. The next is lignite. Remember when we showed the map, a lot of the east is lignite and it slops over into North Dakota. That lignite, some people call it junk coal, but new technologies have been developed that can actually utilize and do coal gasification liquefaction out of the lignite but it does have a high moisture content and lower BTU content and a lesser value.

Governor Schweitzer said the point I want to make is when we are dealing with lignite and those vast resources of lignite technology we have this will never be coal-by-rail. The BTUs are relatively low, 6,500, the moisture content is greater than 30%. This will not be a competitive coal by rail. Our sub-

bituminous coal can be competitive coal-by-rail and our most competitive coal-by-rail would be our bituminous – lowest moisture highest BTU.

Mr. Barrett said I want to hit the generation plants we've been looking at. Obviously, the top, newest technology, the cleanest technology is IGCC power plants. What those are about is producing actually electrical power in a manner that gets the maximum benefit and it captures most of the bad stuff in the processes because they are chemical processes rather than pyrolytic processes, coal-fired processes. California right now is only willing to accept certain power that is produced with this kind of quality where you can capture and sequester, and ultimately sequester, which is an additional level of challenge of the carbon and at the same time they want a blend of other renewables in their power as well. Which is why the wind generation power in combination with this is important.

The Pulverized Coal Power Plant (PC) is the traditional power plant. That is the one that gets all the bad reviews because it pumps all kinds of stuff. This is the oldest technology that has been used. Ninety percent of the power plants in the world are coal-fired like this. That is part of the challenge we have environmentally now and with the market. The market is now turning away from these kinds of plants. The last is the circulating fluidized bed plants. We have one of those in Great Falls under permit application right now, the Southern Montana Electric Group and the Nelson Creek Project in Circle anticipates being a CFB power plant. It is significantly cleaner with the newer technology than pulverized plants but it does not easily allow the capture, particularly of the carbon. When we talk to people we are urging the movement to the IGCC because that is where the market is going. The liquefaction processes are important. Basically when we are going to be making liquid out of this, and the story was out in the *New York Times* that this summer the Air Force will run a B-52 partially on liquefied synthetic fuels as an experiment. This is not pipedream stuff. The Defense Department is putting its foot forward for the first time to actually take the product and put it in a plane and fly it as a comparison mode to the other. Syntroleum is the one producing that. What we're talking about is gasification. The processes are you create a syn gas out of the coal, you take the syn gas and run Fischer-Tropsch out of it. You link two processes together but there are a lot of technicalities in it. These are the main gasifier technologies. The GE is a high-ranked coal, and it appears not to work very well in Montana unless you are using it on our bituminous coal. The same thing with the Conoco-Phillips. The Shell gasifier uses a lower rank of coal but it is not extraordinarily efficient but it can work. The KBR technology is a kind that can use our coals completely. In addition, there is a fifth technology that is owned by an outfit called Sustech. They can use all types of coals, including waste. So what we have to be about is getting private companies to marry their technologies together. Syntroleum is here today and their status is they have a plant that has been producing actively in the United States but with gas and their next step is the conversion to linking the coal into it. Rentech currently has a plant that they are going to be doing in Illinois which is tied into an ammonia plant that will be using coal and converting it into a liquefied product. We have five technologies to turn it to liquid. These five technologies in a business deal have to be combined with the gasification technologies to make a marriage that will work economically given the coal and then given the other economics of the project. This obviously is the reference you were thinking of when you were talking about 70-year old technology, but its has been about 50 years since it has been commercially proven in South Africa after World War II. The Shell was proven in 1993 and they are too busy to care about doing anything in the U.S. right now. They have put a plant up in Cutter and that is all they are interested in doing. This is the outfit that doesn't want to really talk to us. Syntroleum and Rentech have been very active participants in this effort to marry technologies up with the gasification and the Fischer-Tropsch technologies. Those are the kinds of things we've been working on throughout this process. We probably have the best "Rolodex" of names/numbers and companies/individuals and technologies of anyone in the country. We are looking forward to a time here in relatively short order where some of these business partnerships will come together and it won't be pipe dreaming this, these

MINUTES  
June 19, 2006  
Page 31

are significant investments. They aren't necessarily ten billion dollar investments, frankly, a billion and a half investment will probably get you a 10,000 – 15,000 barrel per day operation. When you get into the 80,000 barrels per day you're talking about \$7 billion investment. There are significant job impacts, significant capital costs, significant tax impacts that are positive. They aren't really boondoggles and I think from our perspective and moving forward we are looking forward to being able to put some Montana-owned coal into these processes for the good of the state and hopefully have them announced fairly soon.

Mr. Johnson said I didn't come here today to debate but my remarks with regard to ten years and \$10 billion with regard to 70-year old technology had to do with what I read in the coverage of the Governor's announcement some months ago of his coal-to-fuels initiative and from that coverage the indication was the project was considered to be a ten year-ten billion dollar project. It was going to rely very heavily on Fischer-Tropsch which was according to my research developed in the mid- to late-1930's in Germany. It's that simple. Again, I didn't come to debate and I find all this very exciting. But I think we need to maintain the perspective here.

Mr. Barrett said thank you Mr. Secretary of State, I am hopeful that as we move this forward it is always good that we are all on the same page., that we understand how up-to-date all this new technology is and what the opportunities are so that Montana speaks with one voice when we approach people about investment opportunities. That they see that Montana is all onboard. I hope this has been helpful in terms of broadening everybody's perspective on a lot of the stuff we do. One of the things in business development, we don't often broadcast everything you're doing because in business development you want to let the private side come together and coalesce and put their money together and get ready to rock and roll. Hopefully this helps illuminate the kind of stuff we have been doing.

Governor Schweitzer said by all means to members of the Land Board if you have an interest in any of this coal information and its beyond the scope of what Mary and Monte have and make available to you, please come and see us. We are looking for partners, we are looking for additional information. We don't have all the answers but frankly, in your own words Secretary Johnson, almost all of our decisions have been 5-0 decisions, we've worked very closely together here and there has been little discussion or debate about coal. As I said I think your comments were limited to nine during the last 18 months. We want to work very closely, and when you publicly said you need to know what's going on with Otter Creek, we thought this would be a good opportunity because maybe we haven't spent enough time briefing the Land Board. It was great you brought that up.

Ms. McCulloch said since you gentlemen brought up the issue, and you did mention the number of times the gentlemen on the Land Board have brought up the issue of Otter Creek, as I have made a good point a number of times I am much better at getting things done than talking them to death as I frequently chastise the gentlemen not only on the current Land Board but on the previous Land Board in all good humor of course. But I will remind the Land Board and maybe to the new members of the Land Board that Otter Creek has been something this Land Board has participated in quite actively. More so my first term on the Land Board than this second term. I recall about the first year, 2001, this issue was pretty much deadlocked. It was going nowhere. We were very frustrated in my office and began working with the Northern Cheyenne Tribe. At the time it was Chair Small that we worked with and was very frustrated with the issue. We knew that the first thing that had to happen was that all parties needed to get together so by the end of that year we did bring all members of the Land Board, via their staffers, together in the then-Governor Martz' office. We also brought together the department as well as the Tribe at that time for what was to be a one-day meeting on this issue to get some information ironed out. We also began discussions with Great Northern along this line. What turned out to be not a one-day meeting was

either a two or three-day meeting we were able to iron out many of the issues and had a handshake among all parties to get this going and moving. It was quite historic. Frankly, we probably did step on some toes along the way. We probably did threaten some private self interests along the way as this issue of Otter Creek, which is never very far from my mind, has been at least to my knowledge the only issue that I have as Superintendent of Public Instruction have received a threat over. So you see, Otter Creek is not something that is very far from my mind or very far from you even when I fail to mention it at the meetings here. I just wanted to make sure and remind those on the Land Board of the significance of the Land Board in getting the ball rolling with Otter Creek.

Mr. Johnson said I want to thank the department for a truly comprehensive job on this. And Mr. Barrett's concerns about not want to divulge marketing strategies across the board I certainly understand but I would hope that this would be a learning experience for all of us today and that as we move through this process of developing what is an incredibly important asset to the State of Montana that we would receive periodic briefings without it having to be precipitated by something that perhaps was more confrontational than it needed to be.

Ms. Sexton said we would be glad to do that. As recently as March we did distribute updates as we have contacts with entities. We did distribute updates and we did distribute that on Otter Creek to all Land Board members in March.

Motion to adjourn was made by Mr. McGrath. Seconded by Mr. Morrison.